Purchase of Real Property in the Palo Verde Valley

Real Property and Asset Management Committee
Confidential Item 8-8
July 13, 2015

Current Action

- Authorize the General Manager to purchase land offered by Verbena LLC at a price not to exceed $255,644,000
- Appropriate up to $264,000,000 to complete the transaction

1931 Seven Party Agreement

	MAF
1. PVID (104,500 acres valley)	
2. Yuma Project (25,000 acres)	
3. (a) IID/CVWD	3.850
(b) PVID (16,000 acres mesa)	
4. Metropolitan	0.550
Subtotal	4.400
5. Metropolitan	0.662
Total	5.062
6. IID/CVWD/PVID	0.300
7. Agricultural Use	All Remaining

Post-QSA Allocation

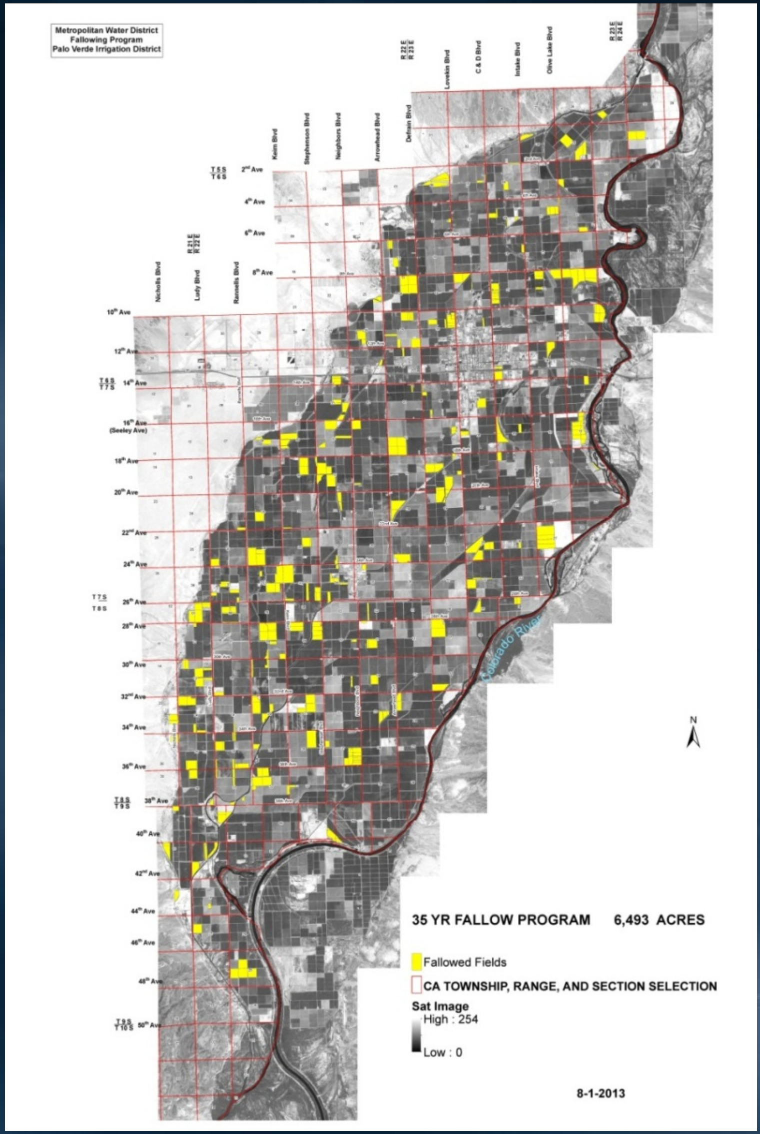
		MAF
1. PVID		0.420
2. Yuma Project		
3. IID/CVWD		3.430
4. Metropolitan		0.550
	Subtotal	4.400
5. Metropolitan		0.662
	Total	5.062

Current Metropolitan Ownership in Palo Verde Valley

- Purchased in 2001 from San Diego Gas & Electric
- Acres Purchased:
  - 9,704 acres in Palo Verde Valley
  - 6,640 acres on the Mesa
- Valley acres are enrolled in the PVID Fallowing Program

PVID Fallowing Program

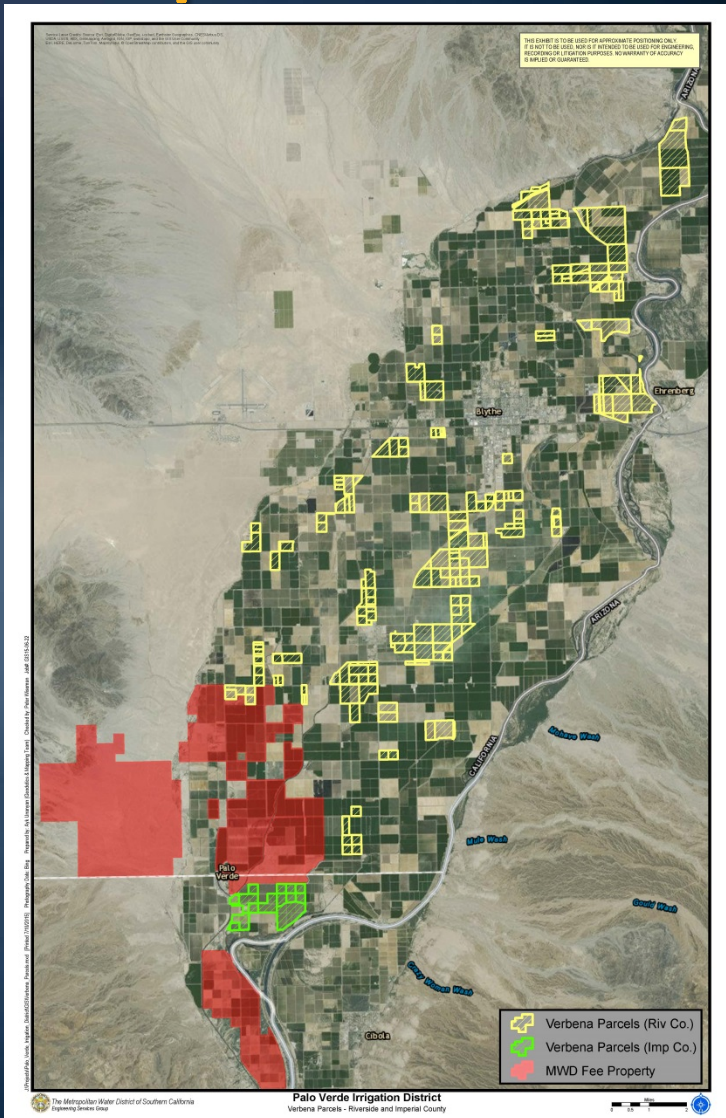
- 35-year program (2005 through 2040)
- Annual water savings: 31,000-132,000 AF
- Program-Qualified Land
    - Priority 1
- Program cap: 26,500 acres (25% of the Valley)
- 25,947 acres enrolled



Expenditures in Palo Verde Cost-to-date

Program Component	Cost
PVID Fallowing Program:	
Upfront Payments	$73.5 M
Annual Payments	$113.9 M
Emergency Fallowing Program	$21.7 M
SDG&E-Purchased Land	$41.4 M
Total Program Cost	$250.5 M

Map of MWD and Verbena Land



- Acres for sale: 12,782.20
- In Palo Verde Valley and eligible for Priority 1 water
- All acres enrolled in the PVID Fallowing Program
- Unit cost/acre: $20,000
- Total cost: $255,644,000

Direct Benefits

- Avoided Cost Analysis
  - Conservative assumption for avoided PVID Fallowing Program costs
  - Cash flow benefit from leasing land
  - Avoided costs of program continuation post-2040
- Analysis Results
  - Results in support for investment in land in the range of $15,000 - $21,000 per acre

Indirect Benefits

- Increases Metropolitan’s flexibility for emergency fallowing
- Reduces risk associated with future program costs
- Reduces risk from outside investors who wish to farm for overseas alfalfa consumption
- Results in an asset that can be leased or sold

Board Options

- Option #1
  - Adopt the CEQA determination that the action is categorically exempt and is not subject to CEQA
  - Authorize the General Manager to purchase the Verbena land at a price not to exceed $255,644,000
  - Appropriate up to $264,000,000 to complete the transaction

Board Options

- Option #2
  - Do not purchase the Verbena land on the terms offered

Recommendation

Option #1

PVID Land Valuation Methodology
Based on Avoided Cost

- Savings from avoided fallowing payments
  - Assumes fallowing at Program's historical rate
- Assumes conservative 4.2 AF/acre yield
- Operate lands as a business
  - Rent at market rates (~3%/year escalation)
  - Refund rental payments when fallowing
  - MWD pays property taxes
- No landholder signup fee for post-2040 renewal
- Can sell land at market prices
- Land Value Result: $15,000 - $21,000 per acre

Detailed Assumptions

Assumptions	Low Range	High Range
Operation Pre-2040	In-line with Current Program (35% enrolled lands)	In-line with Current Program (35% enrolled lands)
Operation Post-2040	In-line with Current Program (35% enrolled lands)	In-line with Current Program (35% enrolled lands)
Operation Post-2040 Cost	*Renew at Current Program*	*Renew at market rates for water*
Avg. Fallowing Calls on enrolled lands Pre-2040	65%	65%
Avg. Fallowing Calls on enrolled lands Post-2040	65%	65%
Salvage value of land	Included	Included
Land Value Escalation	2.5%	2.5%
Discount Rate	5%	5%
County Tax Rate	1.05%	1.05%
County Tax Escalation	2% - Prop 13	2% - Prop 13
PVID Taxes	$8/acre	$8/acre
PVID Tax escalation	3%	3%
Rental Agreements	Current Structure and Rate	Current Structure and Rate
Starting Rent Rate	$250/acre/year	$250/acre/year
Rent Agmt Length	5 years	5 Years
Rent Escalation	16% every 5 years (3.2%/year)	16% every 5 years (3.2%/year)
Fallowing Yield	4.2 AF/Acre	4.2 AF/Acre

Benefits of PVID Land Purchase

- Eliminates future fallowing payments
- Potential water savings on un-fallowed land
  - Reduces the Valley's overall irrigation use
- Reduced need for water purchases at market rates
- Better positioned for end of fallowing program

Benefits and Advantages

Reduces Future Fallowing Payments

- Verbena is a participant in the fallowing program
- Approximately 35% of the land is subject to program fallowing (up to 4,215 acres)
- At maximum fallowing call, about 17,700 acre-feet conserved (applying 4.2 AF/acre rate)
- FY 15-16 payment to Verbena is $3.3 million (would be avoided with purchase)
  - Avoid payments of up to $115 million through 2040

Benefits and Advantages

Potential Water Savings On Un-Fallowed Land

- The un-fallowed land could be farmed with water saving practices
  - Utilize water efficient management techniques
- Plant less water-intensive crops
  - Could save 2.0 AF/acre or more
- Savings potential on un-fallowed land of about 15,600 AF per year (in addition to maximum fallowing call)

Benefits and Advantages

Reduces the Valley's Overall Irrigation Use

- Diversion above 420 TAFY, Metropolitan covers the difference
- Diversions below 420 TAFY, Metropolitan benefits from the savings
- Managing water use on its own land puts Metropolitan in a better position to reduce irrigation use in Palo Verde Valley

Benefits and Advantages

Reduced Need For Market Purchases

- Water saved on Metropolitan-owned land helps avoid additional market purchases of water
- 15,600 AFY potential savings on un-fallowed land
- Potential savings of $5 million to $10 million* in the year of need
  - Based on water transfer price of $300/AF to $650/AF

*Non-escalated dollars

Benefits and Advantages

Better Positioned For End of Fallowing Program

- Current fallowing program runs through 2040
- An extension of the program would require negotiations with PVID and landowners
- After purchase Metropolitan would own approximately 20% of farmland in the Valley
- Better position to negotiate terms of renewal of the fallowing program